

**STATE BOARD OF EQUALIZATION**

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October 26, 1990

Mr. D. A--- H---  
H--- and L--- P--- Co.  
XXXX --- Circle SW  
---, FL XXXXX

Dear Mr. H---:

I am writing in response to your September 8, 1990 letter requesting a legal opinion regarding the applicability of California Sales and Use Tax to "royalty fees" charged by H--- and L--- P--- Corporation (H&L) to its franchisees.

The facts, as I understand them, are as follows. H&L publishes magazines which advertise real property for sale by independent brokers or others. H&L grants exclusive franchises in specified geographical areas for publication and distribution of magazines advertising property within the specified area. A franchisee's income derives from the sale of advertisements to brokers in his or her area. H&L publishes magazines according to the franchisees' specifications regarding format, number of pages, and number of copies. Generally, a franchisee chooses to publish on a monthly or bi-weekly basis. The magazines are eventually distributed to the public free of charge.

The H&L franchisees' pay H&L a fee, based on number of pages, to publish the magazines. In addition to this fee, H&L charges franchisees a "royalty fee" based on a "percentage of the suggested retail sale for the pages of advertising". The "royalty fee" is for "intangible rights such as the exclusive territorial rights, logos, trademarks, etc." Franchisees have a right to print locally, however the royalty fee is charged whether or not H&L does the printing.

H&L has been collecting and remitting California use tax on royalty fees. You have asked us to confirm that "the royalty charges are for intangible rights and not for any tangible personal property and, therefore, are not subject to the State's sales and use tax. We do not concur in your opinion.

Unless specifically excluded or exempted from taxation by statute, all gross receipts from retail sales or purchases for use within this state of tangible personal property are subject to either sales or use tax. (Rev. & Tax. Code § 6051.) Although the legal obligation to pay sales tax is on the retailer, Civil Code Section 1656.1 provides that the retailer may seek sales tax reimbursement from the purchaser. The definition of "gross receipts" includes "any services that are part of the

sale.” (Rev. & Tax. Code § 6012). Services that are part of the sale include any “for which the purchaser must pay as a condition of the purchase and/or functional use of the property.” (Annotation 295.1690. The annotations provide guidance to previous staff decisions.)

As I understand it, H&L presently collects use tax on royalty fees as well as printing charges. This practice is correct. There are only two situations in which H&L would not be obligated to collect a use tax on the royalty fee. The first is where the franchisee does not purchase printing from H&L and the royalty fee is paid absent any transfer of tangible personal property. The second situation is where the printing is itself exempt from use tax. According to our records, some H&L publications qualify for tax exemptions either as “periodicals”, under Rev. & Tax. Code § 6362(a), or as “printed sales messages”, under Rev. & Tax. Code § 6379.5. In these situations, the royalty fee is included as part of those gross receipts exempt from taxation.

Please feel free to contact us again if you have further questions.

Sincerely,

Stella Levy  
Tax Counsel

SL:cl  
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